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USITC Hearing on the United States-Mexico-Canada Agreement
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Summary: The negative employment and wage effects of the current NAFTA arise from the failure to require real labor reform in Mexico. The result has been a fortification of very low wages in Mexico -- which has caused job loss and downward pressure on wages in the U.S. A new trade deal with Mexico must address this core problem directly and forcefully, which cannot occur by relying on changes to rules of origin, labor content rules, dispute settlement procedures or sunset clauses. A comprehensive ITC analysis of the USMCA is important to helping confront this fundamental issue. Failure to rectify the basic flaw in and the major source of controversy over NAFTA 25 years ago will jeopardize support from the new House Democratic majority.

The U.S. International Trade Commission's (ITC) charge to assess the impact of a revised North American Free Trade Agreement (NAFTA), as envisioned in the United States-Mexico-Canada Agreement (USMCA), on the U.S economy and specific industry sectors becomes even more important when you consider the history of this accord. Twenty five years ago there was a failure to effectively assess its impact, characterized by the glowing prediction of President Clinton that NAFTA would generate U.S. jobs "by fostering an export boom to Mexico" and cause a "more rapid closing of the gap between our two wage rates."

The ITC report on NAFTA from 1993 projected that exports from the U.S. to Mexico would rise substantially faster than Mexican imports into the U.S. under the agreement, and that average real wages in Mexico would climb by as much as 16%. These predictions missed the mark substantially because there was a failure to fully account for the pervasiveness of Mexico's industrial policy to attract capital by keeping wages at rock-bottom levels through the lack of labor rights. Instead of converging wages upwards, the trade agreement created the NAFTA paradox: Mexican workers produced more and earned less. Manufacturing productivity increased 80 percent between 1994 and 2011, while real compensation fell almost 20 percent. In the auto sector, Mexican productivity rose 7 percent from 2008 through 2015—despite the Great Recession and its traumas—and median hourly real compensation slid 13 percent, widening the wage-productivity disconnect.

As a result of this disconnect, Mexican hourly workers in the transportation equipment sector—which includes aerospace as well as motor vehicles—earned $2.59 an hour on average in wages in 2017. The hourly wage according to labor contracts ranged from $1 at Mazda and $1.50 at BMW to $3.20 at Nissan. The flip side of these low wages is diminished purchasing power in Mexico and a sharp downward pressure on U.S. wages and jobs.

Mexican wage suppression in turn serves as a magnet for attracting new investment. The U.S. goods trade deficit with Mexico was $71.0 billion in 2017 (the largest ever), and 89% of our deficit in goods traded with Mexico is from vehicles.

In short, while some have claimed NAFTA led to the increase of hundreds of thousands of American industrial jobs, in August 2017 the USTR said "The U.S. Government has certified that at least 700,000 Americans have lost their jobs due to changing trade flows resulting from NAFTA. Many people believe that number is much, much bigger than that."

NAFTA represented the first major trade agreement between high wage, high standard economies and Mexico's very low wage and environmental standards and structures. Reflecting the use of traditional economic trade theory developed before the impact of globalization, there has been considerable lauding of the "integration" of the three economies without taking into account the impact on the daily lives of workers and families in these economies.

To date, much of the discussion on revamping NAFTA has focused on issues that will not directly address the impact on jobs and wages from these vast structural economic differences:

1. Rule of Origin

   This threshold for regional content is raised from 62.5% to 75%. While this change might prevent outsourcing to China, it could potentially increase outsourcing to very low cost Mexico given the regional nature of the requirement. We have already seen a huge exodus of production from the U.S. to Mexico in auto supply companies like Lear and Delphi under the current NAFTA.

2. Labor Value Content (LVC) Provisions

   The new agreement requires 40-45% of the auto content of vehicles shipped from Mexico to be made by workers earning at least $16/hour. There has been a failure to understand that this is unlikely to significantly change the flow of industrial exports from Mexico.

The agreement allows what is essentially a 15% credit for R&D and other elements that occur in the U.S. So in effect the LVC requirement is closer to 25% for motor vehicles. While exact data remains hard to come by, various estimates suggest the vast majority of the millions of vehicles shipped from Mexico already meet that standard, given their amount of U.S. or Canadian content. For example, Mexican Auto Industry Association (AMIA) president Eduardo Solis told a news conference that U.S. content in Mexican parts and components ranged between 37 percent and 39.5 percent, "depending on the scenario."

3. Raising the Mexican Minimum Wage

   There are reports that the new administration in Mexico wants to raise their nation's minimum wage. This will be a positive step but will not address the basic impact of the very low wages in Mexico's industry. "Hourly wages in Mexico in dollar terms are now 40 percent lower than in China. The figure represents a stunning turnaround from just 12 years ago, when labor costs in Mexico were roughly 183 percent higher than China's," according to a report in the Financial Times.

4. Changes in Investor-State Dispute Settlement (ISDS)

   There is considerable controversy regarding the provisions in USCMA and there is a need for reform of the present dispute settlement rules. But if the changes proposed in USCMA are the major strategy of the Administration to make foreign investment less attractive in and reduce outsourcing to Mexico, it is unlikely to have any impact in the immediate future. Indeed, foreign industrial investors have been receiving large scale financial inducements to come to Mexico, rather than having their investments thwarted by arbitrary actions.

5. The Sunset Clause

   Whatever the merits may be of the revised provision for automatic review after a period of a number of years, it is unlikely to lead to addressing here and now the basic economic challenges to the American economy, jobs, and wages.

THE BASIC ISSUE

When I traveled to San Luis Potosi, Mexico this past September I witnessed firsthand a clear example of the basic labor conditions and the industrial structure in Mexico. At the Goodyear plant, production workers are earning in take home pay less than $1.50 an hour for a 9 hour shift with anemic benefits. These workers are laboring under a so-called "protection agreement" entered into by the company and a compliant organization (CTM) with zero negotiating power for the workers. When in protest, they went on strike and many were fired.

In a nearby Continental plant, one of only a few with a real, independent union led by workers, wages are considerably higher, as you can see in a chart attached to my testimony.

There is a real opportunity to chart a new course for trade between the three nations, especially with the election of a new Mexican Congress, and a new Mexican President. Incoming Labor Minister Louisa Maria Alcalde provided further hope of that when she recently said "(protection) contracts are rotten from the outset… it's time for Mexican workers to decide by themselves who should represent them." There is currently legislation being considered in the Mexican Senate which will hopefully totally reverse the wrong direction followed in the old Senate.

Nevertheless, there are powerful forces that would like to see the status quo continue. This speaks to the importance of spelling out specific, detailed steps for change, and a precise delineation of how such requirements will be enforced -- core issues that are not yet fulfilled in the current USMCA. There are tens of thousands of protection agreements in Mexico, backed by compliant unions, and it is vital there be concrete steps toward their termination and toward the ability of Mexican workers to really speak for themselves.

A comprehensive ITC analysis of the USMCA can help us finally confront an issue that has been festering for the last quarter of a century. The failure to do so in the past has created a vacuum easily filled with nostrums and speculation about tariffs, rather than a reconstructed policy on trade that focuses on harmonizing wages upwards and truly supporting good jobs.

It is my belief that without the development of such policy that effectively rectifies the basic flaw in and the major source of controversy over NAFTA 25 years ago, USMCA will not receive strong support among the new House Democratic majority.

The Impact of Effective Worker Rights:

Dramatic differences in pay at Continental and Goodyear Tire Plants in San Luis Potosi, Mexico

	Continental Tire **Independent Union** **Est. 1500 workers**	**Goodyear Tire** **CTM-Controlled Union** **Est. 800 workers**
Average Base Wage	920 pesos/day Approx. $6 USD per hour *	223 pesos/day Approx. $1.32 USD per hour *
**Highest Earned Wage ** **	900,000 pesos annually $48,000 USD a year	215,473 pesos annually $11,584 USD a year
Aguinaldo **(Christmas Bonus)**	44 days' pay = 45,000 pesos or $2,400 USD	26 days' pay = 5,000 pesos or $268 USD
Work Week	5 days 40 hours/week	6 days 54 hours/week
Turnover Rate	1%	Est. 50%

** Continental workers have 8 hour shifts, while Goodyear Tire workers have 9 hour shifts.*

*** While 20% of Continental workers receive the highest wage offered in their wage scale (approximately 300 workers), at Goodyear, we were told there is only 1 position eligible for the highest salary under its wage scale. The average worker at Goodyear makes USD $4,000-5,000 annually.*